87-1564

No. ——

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

NEW YORK STATE DEPARTMENT OF SOCIAL SERVICES,
Petitioner,

v.

OTIS R. BOWEN, SECRETARY,
DEPARTMENT OF HEALTH AND HUMAN SERVICES, *et al.*,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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QUESTION PRESENTED

Can the Department of Health and Human Services retroactively apply its most recent interpretation of an ambiguous statute to require the State of New York to repay 66 million dollars that the Department had disbursed to the State pursuant to the Department's prior and equally permissible interpretation of the statutory ambiguity.

ADDITIONAL PARTIES TO THE PROCEEDING BELOW

In addition to the parties identified in the caption, the Administration for Children, Youth and Families, which is a component of the Department of Health and Human Services, and the Administration's Commissioner, Dodie Livingston, also appeared as defendants. The City of New York appeared in the court of appeals as *amicus curiae* in support of petitioner.

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The New York State Department of Social Services petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. 1a-13a) is reported at 835 F.2d 360. The opinion of the district court (App. 14a-24a) has not been reported.

JURISDICTION

The judgment of the court of appeals (App. 25a) was entered on December 22, 1987. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1) (1982).

STATUTORY PROVISIONS INVOLVED

Section 403(a)(3) of the Social Security Act, 42 U.S.C. § 603(a)(3) (1976), as amended by Pub. L. No. 93-647, § 3, 88 Stat. 2337, 2348 (1975), provided:

> From the sums appropriated therefor, the Secretary of the Treasury shall pay to each State which has an approved plan for aid and services to needy families with children, for each quarter, beginning with the quarter commencing October 1, 1958—
>
> * * * *
>
> (3) in the case of any State, an amount equal to the sum of the following proportions of the total amounts expended during such quarter as found necessary by the Secretary of Health, Education, and Welfare for the proper and efficient administration of the State plan—
>
> (A) 75 percentum of so much of such expenditures as are for the training of personnel employed or preparing for employment by the State agency or by the local agency administering the plan in the political subdivision, and
>
> (B) one-half of the remainder of such expenditures, except that no payment shall be made with respect to amounts expended in connection with the provision of any service described in section 1397a (a)(1) of this title other than services the provision of which is required by section 602 of this title to be included in the plan of the State[.]

Sections 408(d) and 408(f) of the Social Security Act, 42 U.S.C. § 608(d) and (f) (1976), provided:

> (d) services described in paragraph (f)(2) of this section shall be considered as part of the administration of the State plan for purposes of section 603(a)(3) of this title;
>
> but only with respect to a State whose State plan approved under section 602 of this title—
>
> * * * *

(f) includes provision for (1) development of a plan for each such child (including periodic review of the necessity for the child's being in a foster family home or child-care institution) to assure that he receives proper care and that services are provided which are designed to improve the conditions in the home from which he was removed or to otherwise make possible his being placed in the home of a relative specified in section 606(a) of this title, and (2) use by the State or local agency administering the State plan, to the maximum extent practicable, in placing such a child in a foster family home or child-care institution, of the services of employees, of the State public-welfare agency referred to in section 722(a) of this title (relating to allotments to States for child welfare services under sections 721 to 728 of this title) or of any local agency participating in the administration of the plan referred to in such section, who perform functions in the administration of such plan.

STATEMENT

A. Background

This case raises the question of whether the Department of Health and Human Services (HHS) can require the State of New York to return 66 million dollars in grant funds that the Department disbursed to the State pursuant to a reasonable interpretation of an ambiguous statute that was later replaced with a contrary interpretation. The federal program at issue in this case is the foster care component of the Aid to Families with Dependent Children program (AFDC-FC). 42 U.S.C. § 608 (1976).

At all times relevant to this case, Title IV-A of the Social Security Act authorized federal matching grants, in various percentages, for state expenditures both for income maintenance payments to needy families with children and for the costs of administering the state's AFDC plan. 42 U.S.C. § 603(a) (1976). With respect

to foster children, the Act also required the states to provide, as a condition for receiving grants for maintenance payments, caseworkers to assist in the placement of the children and the development of a plan for their proper care and the improvement of conditions in the home from which they were removed. 42 U.S.C. § 608(f) (1976). The Act further provided that these caseworker activities were to be considered administrative costs under section 603(a)(3), which was the principal funding source for all social services provided under the aegis of the Social Security Act prior to 1975. 42 U.S.C. § 608(d) (1976).[1]

In 1975, Congress restructured the AFDC program. Pub. L. No. 93-647, 88 Stat. 2337 (1975). That statute transferred the social service components of Title IV-A to Title XX, including "services for children and adults in foster care." 42 U.S.C. § 1397a(a)(1) (1976). Significantly, federal grants to each state for Title XX programs were limited by a specified appropriations cap, 42 U.S.C. § 1397a(a)(2)(A) (1976), whereas Title IV-A funding remained open-ended. In line with the restructuring of the Act, section 603(a)(3) continued to permit funding for state administrative costs, but was amended with the following proviso: "except that no payment shall be made with respect to amounts expended in connection with the provision of any service described in section 1397a(a)(1) [of Title XX of this Act] other than services [pertaining to the Work Incentive Program]." 42 U.S.C. § 603(a)(3) (1976).

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[1] By its express terms, section 608(d) refers only to section 608(f)(2), which concerns the categories of employees who carry out the activities referred to in section 608(f)(1). But there has never been any question that the costs of all the activities referred to in section 608(f) were to be treated as administrative costs for which matching grants were available under section 603(a)(3). (App. 6a n.5; Court of Appeals Appendix 71, hereinafter "C.A. App. ——.")

As noted above, section 1397a(a)(1) specifically mentions services for children and adults in foster care. Consequently, the 1975 "except" clause to section 603(a)(3) appears to prohibit Title IV-A funding for the caseworker activities mandated by section 608(f). However, Congress did not amend section 608(d) in 1975. Consequently, that section continued to provide that the foster care caseworker activities described in section 608(f) are to be "considered as part of the administration of the State plan for purposes of section 603(a)(3) of this title." 42 U.S.C. § 608(d) (1976). Thus, while the proviso to section 603(a)(3) seems to prohibit funding of foster care activities generally under Title IV-A, section 608(d) seems to retain Title IV-A funding for the cost of caseworker activities. The statute, therefore, presents an interpretive dilemma: should the agency attempt to give effect to both provisions, or should it treat section 608(d) as repealed by implication by section 603(a)(3).

For five years, HHS attempted to give effect to both provisions, and in so doing permitted New York to receive reimbursement for foster care activities in the following way. The agency disbursed funds for social services, including foster care services, under Title XX until New York reached its statutory cap. At that point, the agency reimbursed additional costs for foster care caseworker activities under Title IV-A. (App. 6a-7a.) Under this procedure, which was known as the "AFDC-FC shift," the agency paid to New York approximately $66 million under Title IV-A between 1975 and 1980. (App. 7a.)

New York adopted this procedure at the express instruction of the HHS Regional Office responsible for New York (Region II). In November 1976, Region II disallowed New York's first claim following the 1975 amendments for reimbursement under Title IV-A for expenditures for foster care caseworkers. (App. 9a.) However, on June 13, 1977, Region II reversed itself on the basis of "a policy statement from our Central Office

advising that any activities required by the Federal regulation covering AFDC-FC are reimbursable under Title IV-A." (C.A. App. 85.) A week later, again referring to "material issued by our Central Office indicating that AFDC-FC administrative costs . . . could encompass all activities required . . . for AFDC-FC children," Region II requested New York to submit a revised cost allocation plan "to provide for the transfer to Title IV-A of all AFDC-FC administrative costs incurred by local districts." (C.A. App. 91.) After New York had submitted the revised plan, the Director of the Division of Cost Allocation for Region II formally approved it. (C.A. App. 92-93.) [2]

As the court of appeals found, New York "[d]utifully follow[ed] the Regional Office's suggestion [and] continued its practice of claiming foster care costs under Title XX until its allotment was exhausted, at which time it effected the 'AFDC-FC shift.'" (App. 10a.) Between late 1977 and early 1979, HHS promptly honored these claims, including claims retroactive to October 1, 1975. Beginning in May 1979, HHS began to defer the State's claims. However, the agency never took timely follow-up action as contemplated by the deferral procedures, 45 C.F.R. § 201.15 (1986), nor did it take any steps to amend the approved cost allocation plan. *See* 45 C.F.R. § 95.515(b) (1987). Accordingly, New York drew down the full amount of its claims through September 1980, as it was entitled to do.

Region II was not alone in being advised by the Central Office that expenditures for foster care caseworker activities could be recovered under Title IV-A. In November 1977, the Acting Associate Commissioner of the Office of Family Assistance, which administered the AFDC-FC program, informed the Regional Commis-

[2] HHS regulations provide that the director of the regional division of cost allocation is the official authorized to formally approve a state's cost allocation plans. 45 C.F.R. §§ 95.507, 95.511 (1987).

sioner in Seattle that Title IV-A funds were available for foster care caseworker services. (App. 10a.)

During the relevant period, HHS' Office of General Counsel reached differing conclusions on the interpretive dilemma posed by the 1975 amendments. In February 1977, a staff attorney prepared a memorandum that concluded that Title IV-A funds were not available for foster care caseworker activities. (App. 10a.) That interpretation, however, was rejected in a May 1980 memorandum, prepared at a higher level of the Office of General Counsel in response to questions from the General Accounting Office, that concluded that Title IV-A funds were available for these activities. (App. 11a; C.A. App. 96.)

In June 1981 HHS reversed its 1977 interpretation and issued a formal directive that Title IV-A funds were not available for any foster care caseworker activities. (App. 7a.) The Acting Commissioner of Social Security informed the Secretary of HHS that this decision was based in part on a legal conclusion that section 608(d) had been repealed by implication by the proviso to section 603(a)(3), and in part on the practical consideration that this interpretation provided an opportunity to save $145 million in grant funds for states' prior expenditures under the 1977 interpretation. (C.A. App. 104-05.) [3]

Region II thereafter applied the 1981 directive retroactively to disallow a portion of the funds previously granted to New York. (App. 7a.) When New York ap-

[3] A year before HHS adopted this new interpretation, Congress prospectively resolved the ambiguity created by the 1975 amendments when it again amended the Act to transfer the AFDC Foster Care program from Title IV-A to a new Title IV-E, which went into effect on October 1, 1980. Pub. L. No. 96-272, 94 Stat. 500 (1980). All of the caseworker activities at issue in this case would currently be reimbursable under Title IV-E, even though they remain eligible for funding under Title XX. 42 U.S.C. § 674 (a)(3)(B) (1982). Thus, Congress in effect adopted HHS' 1977 interpretation for the period after October 1, 1980.

pealed, the Departmental Grant Appeals Board affirmed the disallowance on the ground that the 1981 interpretation was the only reasonable construction of the statute. (C.A. App. 176). Region II subsequently disallowed the balance of the prior grants, and New York's appeals were similarly rejected. (App. 7a.)

The effect of New York's reliance on the 1977 interpretation that Title IV-A funds were available for foster care caseworker activities was far-reaching. This interpretation affected the amount of funds spent by counties throughout the State on social service programs. Had Title IV-A funds not been available, the counties either would have had to cut back social services or raise additional funds through taxes.

The impact on New York City was especially great. HHS' 1977 interpretation coincided with the City's financial crisis when both federal and state authorities were working with the City to avoid its bankruptcy. Strict controls were placed on the City's budget, and the City was permitted to proceed with programs only if funding sources were assured. Despite the reduction or elimination of many services funded under Title XX, the City's remaining social services continued to exceed its share of the State's allotment under Title XX. As a result of HHS' interpretation permitting the shift of AFDC-FC expenditures to Title IV-A, the City was able to avoid further cutbacks in its social services for needy children and adults. The bulk of the $66 million in dispute went to New York City (C.A. App. 133), and if the State is ultimately required to return these funds to HHS, the City may be required to make appropriate repayment to the State.

B. Proceedings Below

The State filed an action seeking declaratory and injunctive relief against implementation of the disallowances. The State did not argue that the 1981 interpretation was an impermissible solution to the dilemma presented by the 1975 amendments. Instead, it argued that

the 1977 interpretation was an equally permissible resolution of the statute's ambiguity and therefore it was inappropriate to apply the 1981 interpretation retroactively, particularly in light of HHS' course of conduct and New York's massive reliance on that conduct.

On cross motions for summary judgment, the district court held that it must defer to the view of the Grant Appeals Board that HHS's 1981 interpretation of the statute was the only reasonable interpretation. (App. 22a.) Thus, the district court did not consider New York's arguments that the 1977 interpretation was also reasonable and that it was inequitable to apply the 1981 interpretation retroactively. However, the court observed that "[t]he entire episode . . . reflects no credit on HHS." (App. 23a n.10.) The court further noted that since "New York's reliance" on the 1977 interpretation "had mounted to vast proportions," HHS' conduct "might very well have worked an estoppel upon [HHS] were it a private party." (App. 24a n.10.)

The court of appeals affirmed on a different ground. The court "readily accept[ed] the proposition that the Act is, in pertinent part, ambiguous (if not internally inconsistent), as eloquently attested by the conflicting interpretations adopted by various HHS officials and components . . . ." (App. 8a.) The court also agreed that "the majority view, as it were, favored allowance of the 'AFDC-FC shift.'" (App. 11a.) However, the court found that "notwithstanding various informal statements or representations in favor of permitting reimbursement, there was no *official* HHS interpretation of the statute prior to 1981." (*Id.*, emphasis in original.) This conclusion, the court held, "pretermits the need to address specifically New York's arguments . . . concerning retrospective application of newly-minted agency interpretations." (App. 12a-13a.)

The court reasoned that "in the absence of an official HHS interpretation prior to 1981, the Department's Action Transmittal in that year did not embody a *change*

in the agency's position." (App. 13a, emphasis in original.) Rather, the 1981 interpretation "represented the first official, binding pronouncement on the question, overriding the informal views to the contrary previously articulated within the bureaucracy." (*Id.*) Like the district court, the court of appeals found "nothing commendable in HHS' course of action, redounding as it does to New York's obvious detriment . . . ." (*Id.*) Nonetheless, the court could not "discern any reason in law why the agency's hands must be tied by such informal representations at non-authoritative echelons of the agency's hierarchy." (*Id.*)

REASONS FOR GRANTING THE PETITION

I.

This case presents an important question of general applicability that has been expressly left open in this Court's previous cases involving federal grant programs—can the federal government recover funds that have been disbursed to a state pursuant to a reasonable interpretation of an ambiguous statute that the federal agency later discards in favor of a different resolution of the statutory ambiguity. In *Bennett* v. *Kentucky Department of Education*, 470 U.S. 656 (1985), the Court held that the federal Department of Education could recover funds that had been expended by the state for a purpose that was clearly prohibited by statute. *Id.* at 670-73. In reaching this conclusion, the Court found that there was no ambiguity in the statute, and that the federal Secretary's position was not inconsistent with earlier guidelines provided by the Department. *Id.* at 671-72. However, the Court explicitly noted that "we have no occasion in this case to address the circumstances, if any, in which the Secretary could impose liability for expenditures made in reliance upon an earlier interpretation provided by the Department . . . ." *Id.* at 670. Immediately following this statement the Court cited the pas-

sage in Justice White's concurring opinion in *Bell* v. *New Jersey*, 461 U.S. 773, 794 (1983), which stated that "there is a significant issue whether a State can be required to repay . . . if the claim of violation rests on a new regulation or construction of the statute issued after the State entered the program and had its plan approved." [4]

This case vividly presents the problems foreseen by the Court in *Bennett* v. *Kentucky Department of Education* and by Justice White in *Bell* v. *New Jersey*. The statute at issue here is not merely ambiguous, it is internally contradictory, as the court of appeals noted. (App. 8a.) There is no doubt that the agency charged with implementation of a statute has substantial discretion to resolve such a conflict. *See Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). But the agency cannot fairly interpret the statute one way, provide a state with millions of dollars of desperately needed grant funds over a period of five years, and then demand repayment when the agency later adopts a different interpretation of the statutory ambiguity. Here, as the Court foresaw in *Kentucky Department of Education*, HHS is attempting to "impose liability for expenditures made in reliance upon an earlier interpretation provided by the Department." 470 U.S. at 670. Here, as Justice White foresaw in *Bell* v. *New Jersey*, "the claim of violation rests on a new . . . construction of the statute issued after the State entered the program and had its plan approved." 461 U.S. at 794.

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[4] The Court in *Kentucky Department of Education* also noted that it had no occasion "to decide if a State may be held liable where its interpretation of an ambiguous requirement is more reasonable than an interpretation advanced by the Secretary after the grants were made." *Id.* at 670. The AFDC statute does not give the states the same degree of interpretive responsibility as the education assistance statute at issue in that case. Here New York proceeded under HHS' interpretation of the statutory ambiguity rather than its own.

This Court has recognized "the doctrine that an administrative agency may not apply a new rule retroactively when to do so would unduly intrude on reasonable reliance interests." *Heckler* v. *Community Health Services*, 467 U.S. 51, 60 n.12 (1984). *See SEC* v. *Chenery Corp.*, 332 U.S. 194, 203 (1947). The court of appeals avoided application of this doctrine to the facts of this case by holding that the 1977 interpretation was not sufficiently formal to bind HHS, but this analysis misses the mark in four respects.

First, New York claimed the disputed funds at the explicit direction of HHS' regional office. This was not reliance on the advice of a single low-level office worker, *Schweiker* v. *Hansen*, 450 U.S. 785 (1981), or a private sector intermediary, *Heckler* v. *Community Health Services*, 467 U.S. 51, but rather reliance on a Regional Commissioner whose function is to give the states authoritative guidance on the agency's programs.

Second, the Director of the Division of Cost Allocation in Region II formally approved the new cost allocation plan that incorporated, at the suggestion of another responsible Region II official, the interpretation received from the Central Office. (C.A. App. 92-93.) HHS' regulations specifically provide that the directors of the regional divisions of cost allocation are responsible for approving or disapproving cost allocation plans. 45 C.F.R. §§ 95.507, 95.511 (1987). If the states cannot rely on the approvals of these officials, the regulations are meaningless and the states are left without any source of reliable guidance.

Third, the 1977 interpretation was adopted not merely by a "mid-level official" (App. 11a), but by the Acting Associate Commissioner of the relevant branch of HHS. (App. 10a.) Furthermore, the interpretation was later confirmed by the Office of General Counsel in response to questions from the General Accounting Office. (App. 11a; C.A. App. 96.)

Fourth, and perhaps most important, New York relied not merely on advice that was represented as emanating from a higher level and not merely on the formal approval of its cost allocation plan, but on HHS' actual disbursement of funds that the State then spent. Thus, the State did more than just "[enter] the program and [have] its plan approved." *Bell* v. *New Jersey*, 461 U.S. at 794 (White, J., concurring). HHS' actions in disbursing the funds, after advising New York of its entitlement to them and approving the State's plan, speak louder than any words, and there is nothing at all informal about the disbursement of $66 million in grant funds. Since "[t]he presumption of regularity supports the official acts of public officers," *United States* v. *Chemical Foundation, Inc.*, 272 U.S. 1, 14 (1926), New York was entitled to rely on HHS' knowing disbursements of the funds the agency now seeks to recover. This presumption of regularity and New York's reliance on HHS' disbursements might not have been justified if the payments had been in clear violation of the statute, but it cannot be said that the 1977 interpretation was clearly wrong.[5] This case therefore presents an appropriate oc-

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[5] Since the 1977 interpretation was a permissible reading of the statute, this case is unlike the Court's estoppel cases where parties sought to bind the government to erroneous advice given by one of its agents. *E.g.*, Schweiker v. Hansen, 450 U.S. 785. In such cases, the Court has refused to estop the government on the ground that no official has authority to change the conditions established by Congress to govern the disposition of public funds. *E.g.*, Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380, 385 (1947). That concern, however, is not present in this case. Since the intent of the 1975 amendments with respect to funding for foster care social services is, as the district court said, "occult," (App. 22a), and since the 1977 interpretation was a reasonable attempt to effectuate the congressional intent, it cannot be said that permitting New York to retain the disputed funds will violate Congress' will. This point is underscored by the fact that the 1980 amendments currently in effect permit the use of Title IV funds, over and above Title XX funds, for foster care caseworker services.

casion for the Court to consider the issues of retroactivity and reliance that it has left open in its previous cases involving federal grant programs.

II.

This case also warrants this Court's review because HHS' conduct threatens to undermine the cornerstone of the relationship between the states and the federal government in the operation of grant programs—the ability of the states to make informed decisions, in advance of proceeding with a program, whether to accept the conditions that go along with federal grants. The Court has stressed that grant programs are "in the nature of a contract: in return for federal funds, the States agree to comply with federally imposed conditions." *Pennhurst State School and Hospital* v. *Halderman* 451 U.S. 1, 17 (1981). Under the AFDC-FC program, for example, the states agree, in return for matching grants for income maintenance for needy children and adults in foster care, to provide certain social services to the recipients, for which the federal government also provides matching funds. "Like other federal-state cooperative programs, [the AFDC-FC program] is voluntary and the States are given the choice of complying with the conditions set forth in the Act or foregoing the benefits of federal funding." *Id.* at 11.

The Court has further stressed that the legitimacy of federally imposed conditions "rests on whether the State voluntarily and knowingly accepts the terms of the 'contract.'" *Id.* at 17. However, "[t]here can . . . be no knowing acceptance if a State is unaware of the conditions or is unable to ascertain what is expected of it." *Id.* Thus, the Court has held that "if Congress intends to impose a condition on the grant of federal moneys, it must do so unambiguously" so the states can "exercise their choice knowingly, cognizant of the consequences of their participation." *Id.* (footnote omitted). If those conse-

quences are unpalatable, a state can avoid them by foregoing participation in the program.

Federal agencies must be equally clear in setting forth the terms of participation for the states. If they are permitted to change the conditions for federal grants after a state has received and spent the federal funds, as HHS has done here, they make a shambles of the state's initial decision to participate in the program and upset the balance between the state and federal governments that this Court has found to be critical to the functioning of federal grant programs. Accordingly, this case presents an important question concerning the proper relationship between the states and the federal government in the operation of the nation's extensive system of federal grant programs.

III.

This case also presents a question of significant importance to the citizens of New York and New York City in particular. Under the decision of the court of appeals, the federal government is entitled to recoup the entire $66 million from the State, and a significant portion of this amount is attributable to expenditures made on behalf of the City. Unless the disallowances are reversed, the people of the State and City will bear the ultimate burden for HHS' retroactive application of its flip-flop in interpreting the statute. This Court has granted certiorari "in view of the fiscal importance of the question to [a state]," *Territory of Alaska* v. *American Can Co.*, 358 U.S. 224, 225 (1959), and this case plainly falls within that category of cases which merit the Court's attention.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDICES

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 87-5031

N.Y. STATE DEPARTMENT OF SOCIAL SERVICES,
Appellant

v.

OTIS R. BOWEN, SECRETARY, H.H.S., *et al.*

Appeal from the United States District Court
for the District of Columbia
(Civil Action No. 84-03620)

Argued November 2, 1987

Decided December 22, 1987

Charles A. Miller, with whom *Richard A. Friedman* was on the brief for appellant.

Jaclyn Tanner, Office of the General Counsel, U.S. Department of Health and Human Services, of the Bar of the Court of Appeals of New York, *pro hac vice* by special leave of Court, with whom *Joseph E. diGenova*, United States Attorney, *Royce C. Lamberth*, *R. Craig Lawrence*, *Edith S. Marshall* and *Robert C. Seldon*, Assistant United States Attorneys were on the brief for appellees.

Peter L. Zimroth, Corporation Counsel for the City of New York, was on the brief for *amicus curiae*, The City of New York, urging reversal.

Before: ROBINSON, RUTH B. GINSBURG and STARR, *Circuit Judges.*

Opinion for the Court filed by *Circuit Judge* STARR.

STARR, *Circuit Judge*: This is an appeal from a District Court decision upholding disallowances by the Department of Health and Human Services (HHS) of claims for reimbursement filed by the New York State Department of Social Services. In its claims, New York sought recoupment of costs incurred in providing certain social services to foster children eligible for assistance under the Aid to Families with Dependent Children (AFDC) program, established by Title IV-A of the Social Security Act (the Act), 42 U.S.C. §§ 601-615 (1982 & Supp. III 1985). Reviewing New York's contentions, the District Court deferred to HHS' interpretation of the governing statutory provisions and granted the Department's motion for summary judgment.

Although we disagree with HHS' position that the Social Security Act unambiguously supports only one permissible interpretation, we do agree, more modestly, that HHS' interpretation is reasonable under controlling principles of statutory interpretation. *See Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984); *see also INS v. Cardoza-Fonseca*, 107 S. Ct. 1207 (1987). We further conclude, as to the pivotal question presented on appeal, that the agency's interpretation can lawfully be applied to New York under the circumstances presented. Accordingly, we affirm.

I

The statute in question is mind-numbing in complexity. Happily, the labyrinthine scheme was thoroughly explored by the Departmental Grant Appeals Board in the course of its decision upholding HHS' disallowances. *See New York State Department of Social Services*, No. 449 (July 29, 1983), Joint Appendix (J.A.) at 162 (hereinafter

Board Decision). For our purposes, a brief (albeit inevitably complex) summary of the statute's structure and pertinent provisions will suffice.

A

Title IV-A of the Social Security Act authorizes federal grants to States participating in the AFDC program. 42 U.S.C. §§ 601-615. Participating States are those that have submitted, and had approved by HHS, plans for providing income maintenance payments and social services to needy families. 42 U.S.C. § 601. In 1961, Congress added section 408 to Title IV-A, which provided for federal financial participation (FFP) in state expenditures for the program of interest in this case, namely, Aid to Families With Dependent Children-Foster Care (AFDC-FC). 42 U.S.C. § 608 (1976).[1] The AFDC-FC program not only authorized income maintenance payments on behalf of eligible foster children, but also *required* States to include in these plans certain social services for program beneficiaries. 42 U.S.C. § 608(f).

From at least 1972 to 1975, state expenditures for required foster care services were federally subsidized under section 403(a)(3) of the Act. That section provided for reimbursement of administrative costs necessary for the efficient administration of a Title IV-A state plan. 42 U.S.C. § 603(a)(3). Although the required foster care services would not, standing alone, fit within the rubric of "administration," section 408(d) provided that foster care services described in section 408(f) were to

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[1] In 1980, Congress repealed section 408 and transferred the AFDC-FC program to the newly enacted part E of Title IV, effective at the option of the States as early as October 1980 but no later than October 1982. Pub. L. No. 96-272, 94 Stat. 501 (1980) (Part E codified at 42 U.S.C. §§ 670-676 (1982 & Supp. III 1985)). References to the foster care program, and to all other provisions of the Social Security Act, are to the sections of the Act in effect during the relevant period, i.e., 1975 to 1980.

be considered part of the administration of the state plan for purposes of section 403(a)(3). 42 U.S.C. 608(d). Thus, until 1975 foster care service costs were reimbursed as administrative costs necessary for the administration of a state plan.

B

With that general background, we turn to the amendments of over a decade ago, whose interpretation provides the backdrop of this case. In 1975, Congress broadly restructured social services programs for AFDC recipients. Pub. L. No. 93-647, 88 Stat. 2337 (1975). Congress transferred the social services component of Title IV-A[2] to a newly enacted part of the Social Security Act, Title XX. Title XX, captioned "Grants to States for Services," established a comprehensive program for States' provision of federally subsidized social services. 42 U.S.C. § 1397a (1976). It continued to provide for FFP in state expenditures for these services, but only up to a specified appropriations ceiling or cap. 42 U.S.C. § 1397(a)(2)(A). Included within the broad ambit of Title XX were "services for children and adults in foster care." 42 U.S.C. § 1397a(a)(1).[3]

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[2] The "social services component" of Title IV-A included services States were required to provide for AFDC recipients by section 402(a)(14). 42 U.S.C. § 602(a)(14) (1974). Prior to 1975, section 403(a)(3)(A)(i) of Title IV-A provided for FFP in the costs of these services. The 1975 amendments repealed, *inter alia*, sections 402(a)(14) and 403(a)(3)(A)(i). Pub. L. No. 93-647, § 3(a)(2), 88 Stat. 2348 (1975). Thus, after the 1975 amendments Title IV-A provided for income maintenance payments and activities directly associated with providing beneficiaries with such payments; almost all references to social services had been repealed.

[3] Section 1397a(a)(1)(C) permitted reimbursement for services directed at the goal of "preventing or remedying neglect, abuse, or exploitation of children and adults unable to protect their own interests, or preserving, rehabilitating, or reuniting families." The statute listed foster care as one type of service designed to further this general goal. 42 U.S.C. § 1397a(a)(1).

Consistent with the transfer of Title IV-A's social services provisions to new Title XX, the 1975 amendments altered section 403(a)(3) to eliminate funding under Title IV-A for the costs of nearly all social services. Pub. L. No. 93-647, § 3(a)(3), 88 Stat. 2348 (1975); *see also* H.R. Rep. No. 1490, 93d Cong., 2d Sess. 19 (1974). This result was accomplished by bringing into being the "except clause," which figures prominently in this case. As amended, section 403(a)(3) continued to permit reimbursement of a percentage of state *administrative* costs for AFDC programs (i.e., the costs attendant to providing beneficiaries with income maintenance payments); however, Congress included the following proviso:

> *except* that no payment shall be made with respect to amounts expended in connection with the provision of any service described in section 1397a(a)(1) [of Title XX of this Act] other than services the provision of which is required by [section 402(a)(19) of this Act] to be included in the plan of the State.[4]

42 U.S.C. § 603(a)(3) (emphasis added). Section 1397a(a)(1), which is referred to in the "except clause," expressly mentions foster care services; in consequence, the "except clause" of section 403(a)(3) by its terms appears to prohibit reimbursement for the costs of providing foster care services. Those costs, it would seem, must be claimed only under Title XX.

Notwithstanding the apparent clarity of the "except clause," the new statutory structure was muddied by

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[4] The "services . . . required by [section 402(a)(19)]" are found in subsection (G). Section 402(a)(19)(G) of the Act, 42 U.S.C. § 602(a)(19) (1982 & Supp. III 1985), refers to social and supportive services necessary to enable certain AFDC recipients to accept employment or receive manpower training under the Work Incentive Program (or "WIN" program). The WIN program was established by Title IV-C of the Act, 42 U.S.C. §§ 630-645 (1982 & Supp. III 1985).

virtue of a remnant from the pre-1975 regime, section 408(d). That provision states that certain foster care costs *are* reimbursable under section 403(a)(3). As noted above, under section 408(d) foster care activities (described in subsection 408(f)) are to be "considered as part of the administration of the Senate plan for purposes of [section 403(a)(3)]." 42 U.S.C. § 608(d).[5] Since the only purpose of section 403(a)(3) is to provide for federal matching of particular state AFDC expenditures, section 408(d) appears to instruct the federal government to reimburse States for the designated foster care services as administrative costs of the state plan.

C

In the uncertainty engendered by these maze-like provisions, New York and several other States continued to budget expenditures on foster care services in the belief that reimbursement under Title IV-A would be forthcoming. The practice adopted by New York in the wake of Title XX's enactment came to be known as the "AFDC-FC shift." Board Decision, *supra* p. 3, J.A. at 166; Brief for Appellant at 14-15. The technique worked this way. New York claimed (and received) reimbursement for social services under Title XX until the State reached the statutory cap. When the Title XX cap was reached,

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[5] Section 408(d) specifically refers only to subsection 408(f)(2), which describes the categories of employees who are to carry out, to the extent practicable, the activities specified in subsection 408(f)(1). Thus, under a literal reading of section 408(d), States could obtain reimbursement under 403(a)(3) only for the costs associated with the employees described in subsection 408(f)(2) rather than for all the costs of the services themselves. It appears, however, that prior to 1975 the agency permitted FFP in the costs of all the activities referred to in subsection 408(f). *See* J.A. at 71; Brief for Appellees at 4.

New York then switched from Title XX to claim the unreimbursed social service costs under Title IV-A.[6]

Six years after the 1975 amendments, HHS published an agency-wide directive elucidating the operation and interplay of the provisions at issue. Under HHS' interpretation, the "AFDC-FC shift" was impermissible; FFP was, in the agency's view, *not* available for foster care cost recovery under Title IV-A. Aid to Families with Dependent Children Action Transmittal, SSA-AT-81-18 (June 24, 1981), J.A. at 117. In October 1981, the HHS Regional Office applied this determination to disallow one of New York's claims. New York appealed to the Departmental Grant Appeals Board, which in July 1983 affirmed the disallowance. Subsequently, two other claims were disallowed and similarly affirmed. This litigation followed contesting the disallowances, which amount to approximately $66 million.

II

New York argues that the foster care services which it provided remained eligible for matching grants as "administrative costs" under section 403(a)(3). In New York's view, the "except clause" precludes only payment for *services* described in Title XX and does not directly address the status of such services that also qualify, pursuant to section 408(d), as *administrative costs*, under Title IV-A. Brief for Appellant at 30-31. Unpersuaded by New York's interpretation, the Board construed the "except clause" flatly to prohibit FFP in the costs of state foster care service activities regardless of whether the costs could also be considered administrative costs.

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[6] It bears noting here that Title IV-A offered a lower percentage of reimbursement (fifty percent, as compared to the seventy-five percent provided under Title XX), but it had the singular advantage of having no cap.

The apparent inconsistency infecting the statute's various provisions need not detain us. We readily accept the proposition that the Act is, in pertinent part, ambiguous (if not internally contradictory), as eloquently attested by the conflicting interpretations adopted by various HHS officials and components, which we shall describe presently. Indeed, in this appeal New York has not contested the validity of HHS' 1981 determination that foster care activities are *not* reimbursable under Title IV-A of the Act; instead, the State insists that this interpretation, albeit reasonable, may not permissibly be applied to it. Relying on internal memoranda and a letter from HHS' Region II (the field office charged with overseeing the Empire State), New York contends that HHS "officially" interpreted the "except clause" in 1977 to permit reimbursement of foster care service costs. Brief for Appellant at 11-13. That being the case, the State argues, the contrary interpretaiton embodied in HHS' 1981 Action Transmittal represented a change in the agency's interpretation of the statute, the retroactive application of which is "arbitrary and capricious" within the meaning of a familiar provision of the Administrative Proceduce Act, 5 U.S.C. § 706(2)(A) (1982). *Id.* at 39-41. Specifically, New York argues that the factors identified by this court in *Retail, Wholesale and Department Store Union, AFL-CIO v. NLRB*, 466 F.2d 380 (D.C. Cir. 1972), as recently elucidated by the court *en banc* in *Clark-Cowlitz Joint Operating Agency v. FERC*, 826 F.2d 1074 (D.C. Cir. 1987), relating to the permissibility of a *retroactive application* of a new agency interpretation, preclude application of HHS' 1981 interpretation to New York's pre-1981 claims. *Id.* at 40, 48.

III

The history of the agency's treatment of this question during the relevant period unmistakably reveals inconsistency within HHS as to New York's claims generally and, more specifically, the import of the "except clause."

To begin at the beginning: In November 1976, Region II disallowed New York's first claim following the 1975 amendments for reimbursement of foster care costs under Title IV-A. The Regional Office grounded its disallowance on the State's failure to allocate its claimed costs between income maintenance and social services activities as required by HHS regulations. *See* 45 C.F.R. § 232.30 (1976). Region II did not, however, mention the "except clause" of section 403(a)(3) as a basis for its decision.

In June 1977, the Regional Office had a change of heart. Region II sent New York an informational copy of its recommendation to the Central Office that the November 1976 disallowance of New York's claim be withdrawn. Memorandum from William Toby, Regional Commissioner Region II (June 17, 1977), J.A. at 85 (hereinafter Toby Memorandum). Also enclosed in the Region's correspondence was an informational copy of a May 18, 1977, memorandum that apparently induced the Region's change in position. The one-page memorandum from one Mildred Hoadley, then Director of Income Maintenance Policy in the Assistance Payments Administration in HHS' Central Office in Washington, D.C., to an Associate Regional Commissioner in California, asserted, without mentioning section 403(a)(3), that "a State may claim [reimbursement] under title IV-A for carrying out any provision required in title IV-A." Memorandum from Mildred Hoadley, Director, Division of Income Maintenance Policy (May 18, 1977), J.A. at 86 (hereinafter Hoadley Memorandum). Citing the Hoadley Memorandum, Region II stated in its recommendation to the Central Office that "any and all of the activities performed by service workers for AFDC-FC children in New York and claimed for in the disallowance claim are allowable." Toby Memorandum, *supra* p. 9, J.A. at 85. According to New York, this communication represented the agency's first official interpretation of the amended Act. Brief for Appellants at 12.

Shortly after informing New York of its intention to reconsider the 1976 disallowance, the Regional Office instructed New York to revise its Title IV-A cost allocation procedure. J.A. at 91. Region II stated that all AFDC-FC activities could be claimed as administrative costs reimbursable under section 403(a)(3), referring to the Hoadley Memorandum. *Id.* Dutifully following the Regional Office's suggestion, New York continued its practice of claiming foster care costs under Title XX until its allotment was exhausted, at which time it effected the "AFDC-FC shift." Some of its Title IV-A claims were paid, while "[o]thers remained in various stages of bureaucratic limbo for the next four years." *New York State Department of Social Services v. Bowen*, No. 84-3620, mem. op. at 7 (D.D.C. Nov. 21, 1986).

As might be expected in a vast bureaucracy, not all components within HHS embraced the interpretation articulated by Ms. Hoadley and Region II. In fact, prior to distribution of Ms. Hoadley's one-page analysis, another component of HHS produced a more extensive memorandum setting forth a contrary interpretation. This interpretation appeared in a February 1977 memorandum produced in HHS' Office of General Counsel and distributed to the Acting Commissioner of the Assistance Payments Administration. Memorandum from Ronald N. Sutter, Attorney, Office of General Counsel (Feb. 23, 1977), J.A. at 70. Examining the statute's background, language, and the legislative history of the 1975 amendments, the memorandum concluded that funding "is clearly unavailable for the services described in section 408(f)(1)" and "the better reading of the statute" precludes funding under section 408(f)(2). *Id.*

In November 1977, however, the Acting Associate Commissioner, the recipient of this memorandum, stated in a one-page letter to the Regional Commissioner in Seattle that Title IV-A funds *are* available for the ad-

ministrative costs of the States' foster care programs. J.A. at 90. Similarly, the Office of General Counsel subsequently rejected the 1977 memorandum's conclusion that the "better reading" of the statute precludes funding for services described in section 408(f)(2). J.A. at 96, 101-03.

Thus, the pre-1981 history of the treatment of this narrow issue reveals that there were various and conflicting interpretations of the statute within HHS. To be sure, the majority view, as it were, favored the allowance of the "AFDC-FC shift." But more fundamentally, a dispassionate examination of the facts supports the following conclusion: notwithstanding various informal statements or representations in favor of permitting reimbursement, there was no *official* HHS interpretation of the statute prior to 1981. No authoritative pronouncement in the form of an Action Transmittal or other formal agency statement of position was forthcoming until that later time.

New York is, of course, of a different view. The State asserts that the Hoadley Memorandum, in conjunction with Region's II's actions, represented the official HHS position on the issue. We cannot agree. The memorandum on its face represented only the recapitulation of a telephone conversation between two mid-level agency employees. Hoadley Memorandum, *supra* p. 9, J.A. at 86. This rather abbreviated interpretation contained no statement of the statutory or regulatory basis for its stated conclusion; indeed, it did not even mention the "except clause" specifically or section 403(a)(3) more generally. *Id.* This is informality in the extreme. In addition, we have been referred to nothing supporting the remarkable proposition that a mid-level official enjoyed the authority to issue an official HHS interpretation in an informal memorandum. New York points to no statute, regulation, or written policy statement indicating that

this odd source of policymaking authority did in fact exist.[7]

The decidedly informal procedure used to arrive at this interpretation contrasts sharply with the process that culminated in the agency's position officially articulated in 1981. The 1981 interpretation was predicated on a lengthy memorandum setting forth a thorough analysis of the arguments for and against each position. And the position it settled upon was embraced by high officials in the Department. After reviewing the various interpretive options, the Acting Commissioner of Social Security opted in favor of the now-challenged interpretation, which was then forwarded to the Office of the General Counsel for review and approval. The Commissioner of Social Security duly informed the Secretary of HHS in writing of his position. Finally, and importantly, the interpretation was thereafter memorialized in an Action Transmittal, which we are informed is one of the established vehicles for the formal memorialization and communication of official agency policy. *See* SSA-AT-78-28 (Action Transmittal setting forth the procedures to be followed for issuances of policy statements to States) (noted in Board Decision, *supra* p. 3, J.A. at 180). This, then, represented formal agency action upon which affected parties could reasonably rely, in contrast to the informal, non-authoritative nature of what had gone before.

Our conclusion that the actions of the agency prior to 1981 did not rise to the level of an official agency interpretation pretermits the need to address specifically New York's arguments under the *Retail, Wholesale-Clark Cowlitz* line of authority concerning retrospective

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[7] In other settings, Congress has, in effect, delegated to certain agency employees the authority to issue interpretations or approvals that are binding on the agency if promulgated in conformity with established procedures. *See* 15 U.S.C. § 1640(f) (1982) (reliance on official Federal Reserve Board staff interpretations or approvals provides creditors with good faith defense to liability).

application of newly-minted agency interpretations. It is manifest that, in the absence of an official HHS interpretation prior to 1981, the Department's Action Transmittal in that year did not embody a *change* in the agency's position. Instead, it represented the first official, binding pronouncement on the question, overriding the informal views to the contrary previously articulated within the bureaucracy. Although we find nothing commendable in HHS' course of action, redounding as it does to New York's obvious detriment, we cannot discern any reason in law why the agency's hands must be tied by such informal representations at non-authoritative echelons of the agency's hierarchy.

For the foregoing reasons, the District Court's judgment is

Affirmed.

APPENDIX B

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 84-3620

NEW YORK STATE DEPARTMENT OF SOCIAL SERVICES,
Plaintiff,

v.

OTIS R. BOWEN, Secretary, *et al.*,
Defendants.

[Filed Nov. 21, 1986]

MEMORANDUM AND ORDER

This case entails a dispute between the State of New York and the federal government over which is to bear the cost of some $66.3 million spent by plaintiff New York State Department of Social Services ("DDS") in providing certain social services to foster children receiving funds from the Aid to Families With Dependent Children-Foster Children ("AFDC-FC") program under the Social Security Act. Although aware of a pervasive uncertainty as to the matter as early as November, 1976, it was not until mid-1981 that defendant United States Department of Health and Human Services ("HHS") got around to publishing an agency-wide directive declaring that the states were no longer entitled to federal reimbursement for some of their expenditures for such services following major revisions of the Social Security Act in October, 1975. In the meantime, New York, as

well as other states, had continued to provide the services in a misbegotten expectation of eventual reimbursement for which it blames HHS. When one of its claims (for approximately $8.5 million) was officially disallowed in October, 1981, New York appealed to HHS' Departmental Grant Appeals Board (the "Board"), which, in July, 1983, affirmed the disallowance. Other claims were later disallowed and similarly affirmed. The parties agree that the several decisions of the Board constitute final agency action with respect to each, and that all are now properly before this Court for review pursuant to the judicial review provisions of the Administrative Procedure Act ("APA"), 5 U.S.C. §§ 701-06 (1982).

New York seeks declaratory and injunctive relief, contending that the Board's decisions erroneously interpreted the governing statutory law; that HHS inequitably gave retroactive effect to the 1981 directive prohibiting reimbursement, the seemingly authoritative intimations DSS had received to the contrary over the preceding four years having accurately reflected an earlier official agency policy which the 1981 directive reversed; and that the 1981 directive was, in any case, a legislative rule which required notice-and-comment before it could become effective at all. The case is now before the Court on cross-motions for summary judgment. The issue upon which the Court makes disposition of the case being entirely one of law, for the reasons hereinafter set forth plaintiff's motion for summary judgment will be denied, defendant's motion will be granted, and the amended complaint dismissed with prejudice.

I.

The complex, intricately interrelated statutory scheme under which this controversy arises is meticulously described by the Board in its Decision No. 449, No. 82-117-NY-HD of July 29, 1983 (R. 302-327), and its exposition in full is not relevant for present purposes. In brief and oversimplified summary, from 1961 through 1975 the

federal government undertook to subsidize the states' expenditures for certain social services it required the states to furnish its children in foster care who were receiving AFDC income maintenance payments under Title IV-A of the Social Security Act (the "Act"), 42 U.S.C. §§ 601-15 (1982), e.g., their placement in suitable foster homes and development and oversight of appropriate plans of foster care.

Effective October 1, 1975, Congress amended the Act by adding Title XX, which established a comprehensive program for the provision of social services generally. Pub. L. No. 93-647, 88 Stat. 2337 (1975) (current version at 42 U.S.C. § 1397 (1982 & Supp. III 1985)).[1] Section 2002(a)(1) of the new statute authorized federal financial participation in state expenditures for various services to the needy directed at certain statutorily prescribed goals, several of which embraced foster care for children, e.g., preventing child abuse or neglect and preserving the integrity of families. 88 Stat. at 2337-43. Title XX also established an appropriations cap limiting the amount of federal money which could be expended, and prescribed a formula by which a maximum annual allotment for each state would be calculated. *Id.*

At the same time it added Title XX to the Act, Congres aiso amended the section of the Act that authorized payment to the states for their Title IV-A administrative expenses, including AFDC-FC. Pub. L. No. 93-647 § 3, 88 Stat. 2337, 2348 (1975). As amended, section 403(a)(3) of the Act still authorized reimbursement of a percentage of a state's *administrative* costs for AFDC, with, however, a proviso:

> . . . except that no payment shall be made with respect to amounts expended in connection with the

[1] Title XX has been amended a number of times since 1975. All references to Title XX herein are to the statute in effect from 1975 to 1981.

> provision of any service described in section [2002 (a)(1) of this Act] other than services the provision of which is required by [section 402(a)(19) of this Act] to be included in the plan of the State . . . .

42 U.S.C. § 603(a)(3) (1976) (current version at 42 U.S.C. § 603(a)(3) (1982)).[2] It is the significance to be ascribed to the "except clause" that lies at the heart of the current controversy: specifically, whether Congress intended it to bar even non-duplicative reimbursement for administrative costs associated with *social* services (except for the WIN program) under Title IV-A.

New York submits its claims for reimbursement to Region II, the field office of HHS overseeing New York. After Title XX went into effect, DSS routinely began to make claims for each county for the social services rendered by foster care caseworkers under Title XX until the state's allotment under that title was exhausted, then it claimed the remainder under Title IV-A, at a lower rate of reimbursement, but without a cap. In November, 1976, the Regional Office disallowed DSS' first claim (for about $1.3 million), citing as the reason what might have been merely an accounting error: DSS' failure to allocate costs between income maintenance and social services activities.[3] DSS asked for a reconsideration in April, 1977.

Then, on June 17, 1977, the Regional Office sent DSS an informational copy of a one-page "memorandum," dated May 18, 1977, from a Mildred Hoadley, then di-

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[2] Section 402(a)(19)(B) of the Act, 42 U.S.C. § 602(a)(19)(B) (1982), refers to social and supportive services necessary to enable certain AFDC recipients to accept employment or receive manpower training under the Work Incentive Program ("WIN") established by Title IV-C of the Act, 42 U.S.C. §§ 630-45 (1982 & Supp. III 1985).

[3] Published regulations required claimants to allocate separately their costs for income maintenance and social services activities when claiming reimbursement under Title IV-A. 45 C.F.R. § 232.30 (1976), *as amended*, 47 Fed. Reg. 17,508 (1982).

rector of HHS' Division of Income Maintenance Policy, Assistance Payments Administration, at HHS' Central Office in Washington, D.C.,[4] to an associate regional commissioner in California, purporting to advise the latter, in response to a query, that "a State may claim [reimbursement] under [T]itle IV-A for carrying out any provision required in [T]itle IV-A."[5] Accompanying the memorandum was an informational copy of a Region II Office recommendation to the Central Office that the November, 1976, disallowance of DSS' claim be withdrawn.

A few days later, a Region II associate commissioner advised DSS (apparently on the basis of the Hoadley memorandum) to amend its Title IV-A cost allocation procedure to classify all AFDC-FC activities, whether related to income maintenance or social services, as reimbursable "administrative" costs. DSS relied upon this apparently authoritative instruction, did as suggested, and assumed henceforth that all doubt had been resolved that it could properly claim reimbursement under Title IV-A for all services its caseworkers rendered, including social services for its AFDC children in foster care, after exhausting its Title XX allotment, which it then proceeded to do for each of the years in issue here.[6] Some

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[4] The agency was, at the time, called the Department of Health, Education, and Welfare.

[5] HHS dismisses the memorandum as nothing more than a "memorialization" of a telephone conversation between Hoadley and the associate regional commissioner, which did not purport to make any analysis of the law whatsoever. New York maintains that the memorandum is, in effect, an "official" reflection of HHS "policy," or its equivalent, which DSS reasonably viewed as such.

[6] New York submits that reliance was particularly poignant in its case, because New York City was at the time on the verge of bankruptcy. Without the anticipated Title IV-A funding, the City would have been forced to reduce its other services expenditures or raise additional tax revenues, or both, to cover its AFDC-FC expenses. New York City ultimately incurred approximately three-quarters of the currently disallowed expenditures.

of its claims were promptly paid without question. Others remained in various stages of bureaucratic limbo for the next four years.

Finally, on June 24, 1981, HHS issued "Action Transmittal SSA-AT 81-18," the pronouncement HHS contends represents its first "official policy" statement on the subject, declaring that states could *not* claim reimbursement for any of its caseworker social services to foster care children under Title IV-A (although Title IV-A still required that they be provided) on the ground that the "except clause" prohibited payment for any such services, and had done so since it was enacted in 1975. The Action Transmittal concluded: "[s]tate plans and cost allocation plans that allow costs for these services under [T]itle IV-A have been approved in error. HHS Regional Offices will be acting to disallow [reimbursement] under [T]itle IV-A where such claims have been paid or deferred."

On October 20, 1981, HHS notified DSS that it was disallowing one of its Title IV-A claims for foster care social service costs incurred between July, 1976, and March, 1979, totalling approximately $8.6 million. In July, 1982, New York appealed the disallowance to the Grant Appeals Board, but the Board's Decision No. 449 upheld the disallowance on July 29, 1983, in the comprehensive ruling that became the basis for all disallowances at issue here. On November 28, 1984, DSS filed this action seeking judicial review of Decision Nos. 449 and 552, later amending its complaint to include a challenge to Decision No. 614.[7]

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[7] On November 28, 1983, HHS notified DSS that it had redisallowed DSS' initial claim for the $1.3 million in costs incurred between October 1 and December 31, 1975. Again, after DSS' appeal, the Board upheld the disallowance on July 16, 1984 (Decision No. 552). Finally, on June 27, 1984, HHS notified DSS of the disallowance of an additional $56 million in costs incurred between January, 1976, and September, 1980, and the Board, on December 20, 1984, once again upheld the disallowance. (Decision No. 614).

II.

In its appeal of HHS' disallowances New York was represented throughout by the able counsel who are appearing for it here, and the same arguments (and another—estoppel—since abandoned) were thoroughly briefed and presented to the Board. The Board rendered its own equally thorough analysis of the Act in its 27-page Decision of July 29, 1983, in which it found, *inter alia*, the language of the "except clause" to be unambiguously definite in its prohibition of the reimbursements DSS was seeking.

The interpretation given the Act by HHS, the agency charged with administering the expenditures it authorizes, is entitled to "substantial deference" by a reviewing court. *Blum* v. *Bacon*, 457 U.S. 132, 141 (1982). If the agency has considered the relevant factors, and its reasoning is thorough and consistent, a reviewing court may not substitute its judgment for that of the agency, *Center for Auto Safety* v. *Peck*, 751 F.2d 1336, 1342 (D.C. Cir. 1985) (citing *Motor Vehicle Mfrs. Ass'n.* v. *State Farm Mutual Auto. Ins.*, 463 U.S. 29, 43 (1983)); *Federal Election Comm.* v. *Democratic Senatorial Campaign Comm.*, 454 U.S. 27, 37 (1981), nor may it adopt its own construction of the agency's governing statute in preference to the agency's if the latter's is reasonable. *Connecticut Dept. of Income Maintenance* v. *Heckler*, 105 S. Ct. 2210, 2215 (1985).

The Supreme Court has stated that "the starting point for interpreting a statute is the language of the statute itself," and "[a]bsent a clearly expressed legislative intention to the contrary, that language must ordinarily be regarded as conclusive." *Consumer Prod. Safety Comm.* v. *GTE Sylvania*, 447 U.S. 102, 108 (1980). The text of the statute thus being clearly a "relevant factor," and the Board's literal reading of it certainly a reasonable, although harsh, one (for New York's purposes), this

Court must give it the deference that is its due, unless there appears a "clearly expressed legislative intention to the contrary."

New York contends that the legislative intention with respect to the October, 1975, amendments is sufficiently obscure to have admitted of agency interpretation. As the Court of Appeals for this Circuit has observed, an agency's "shifting interpretation of its statutory authority bespeaks of an ambiguity in the statute's language and legislative history." *Process Gas Consumers Group* v. *United States Dept. of Agriculture*, 694 F.2d 778, 792 (D.C. Cir. 1982) (*en banc*) (footnote omitted), *cert. denied*, 461 U.S. 905 (1983). According to New York, until June of 1981, when HHS issued its Action Transmittal 81-18 declaring foster care caseworker social services under Title IV-A to be nonreimbursable, HHS' officials at both national and local offices had officially "interpreted" the legislation otherwise. New York argues, therefore, that Action Transmittal 81-18 represented an interpretive shift in HHS' reading of ambiguous legislation, one it may have been entitled to make, but which was nevertheless a "policy change," the retroactive application of which, the argument continues, to disallow its expenditures of some six years past would, in the circumstances, be inequitable. *See SEC* v. *Chenery Corp.*, 332 U.S. 194, 203 (1947); *Retail, Wholesale and Department Store Union* v. *NLRB*, 466 F.2d 380, 390 (D.C. Cir. 1972).[8]

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[8] New York has submitted affidavits of Mildred (Hoadley) O'Keefe and Florence Aitchison, the Region II associate commissioner from 1969-80, both now retired from government service, attesting to their perceptions of a consensus within the agency between 1975 and 1981 that social services costs remained reimbursable under Title IV-A. HHS has moved to strike the affidavits on the ground that they were not a part of the administrative record before the Board, and, thus, are not properly before the Court in its review of the Board's decision. *See Citizens to Preserve Overton Park, Inc.* v. *Volpe*, 401 U.S. 402, 419-20 (1971); *see also Formula* v.

The Grant Appeals Board, however, did not stop with a careful reading of the 1975 legislation itself. It also examined the legislative history, such as it is, as well as the entire statutory mechanism by which Congress has sought to apportion the costs of AFDC and related social services between state and federal governments. It found nothing in either to suggest that its reading of the "except clause" was out of harmony with the remainder; Congress had all along intended exactly what it said, leaving no ambiguity open to agency interpretation. The Court finds the Board's reasoning to be logical, its method appropriate to the ascertainment of an occult legislative intent, and once again concludes that it must accept the result the Board reached, whether or not it would have done likewise on its own.[9] *See Chevron* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 & n.11 (1984).

Heckler, 779 F.2d 743, 745 n.2 (D.C. Cir. 1985). The tenor of both affidavits, however, is merely to make express what is implicit in the administrative record, viz., that some mid-level HHS officials were under the foregoing impression notwithstanding the 1975 amendments to the Act, and that those officials shared their impressions with one another and with their client states. In the light of the disposition made of the case on the merits, the motion to strike will be denied as moot.

[9] At least one other court has *de novo* agreed with the Board as to the correct statutory interpretation. *See Oregon Dept. of Human Resources & Children's Servs. Div.* v. *Heckler*, No. 83-1466 (D. Or. Jan. 31, 1984).

New York also contends that Action Transmittal 81-18 constituted a legislative rule-making requiring formal notice-and-comment pursuant to the APA, 5 U.S.C. § 553 (1982).

The notice-and-comment procedures of the APA do not apply, however, to an agency's "interpretative rules." 5 U.S.C. § 553(b)(3)(A). There can be no question that Action Transmittal 81-18 was as interpretative rule, as that term has been defined by the D.C. Circuit:

> Generally speaking, it seems to be established that 'regulations,' 'substantive rules' or 'legislative rules' are those which create law, usually implementary to an existing law; whereas

Equities notwithstanding, no "policy," however salutary, venerable, or "official," can be enforced in contravention of an express statutory command. Agencies are simply not entitled to do what they are not authorized by statute to do, no matter how reasonable it may seem to them, or to a court, that they be allowed to do it. *See American Bankers Ass'n* v. *SEC*, No. 85-6055, slip op. at 23 (D.C. Cir. November 4, 1986). The Board found that in 1981 HHS had belatedly discovered a misapprehension on the part of some of its personnel as to what the statute permitted and corrected it. This Court has accepted the Board's conclusion as to the purport of the legislation. There are, therefore, no equities to balance. The language of the statute is mandatory; HHS officials never had authority or discretion to give dispensation from it, and, unfortunately for New York, the rule is that "those who deal with the Government are expected to know the law and may not rely on the conduct of government agents contrary to law." *Heckler* v. *Community Health Servs.*, 104 S. Ct. 2218, 2226 (1984) (footnote omitted). Even if there are exceptions to the rule, there is no evidence of the "affirmative misconduct" of government officials which would be necessary, at a minimum, to justify a departure from it. *See id.* at 2228 (Rehnquist, J., concurring).[10]

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interpretative rules are statements as to what the administrative officer thinks the statute or regulation means.

Gibson Wine Co. v. *Snyder*, 194 F.2d 329, 331 (D.C. Cir. 1952), *quoted in Cabais* v. *Egger*, 690 F.2d 234, 238 (D.C. Cir. 1983). The APA does not require an agency to hold a referendum each time it reads a statute to see if public agrees with it.

[10] The entire episode, however, reflects no credit on HHS. From 1976 forward responsible officials knew that several states, at least those with social services costs approaching reimbursable limits under Title XX, were anxious to know whether they could continue to incur them with expectations of further reimbursement of some of them under Title IV-A. Both claims and disallowances were awaiting decisions. Yet no one at HHS made a definitive reading

The Board's decision being rational and in accordance with law, for the foregoing reasons, therefore, it is, this 21st day of November, 1986,

ORDERED, that plaintiff's motion for summary judgment is denied; and it is

FURTHER ORDERED, that defendant's motion for summary judgment is granted, and the amended complaint is dismissed with prejudice; and it is

FURTHER ORDERED, that defendants' motion to strike is denied as moot.

/s/ Thomas Penfield Jackson
THOMAS PENFIELD JACKSON
U.S. District Judge

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of the statute, much less a request of Congress for clarification, until New York's reliance upon the misleading signals it had been given had mounted to vast proportions. HHS' inexplicable neglect of its obligation to make a decision expeditiously was arguably more injurious to New York than an early adverse decision itself could ever have been, and might very well have worked an estoppel upon it were it a private party.

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 87-5031

N.Y. STATE DEPARTMENT OF SOCIAL SERVICES,
Appellant,

v.

OTIS R. BOWEN, SECRETARY,
DEPARTMENT OF HEALTH AND HUMAN SERVICES, *et al.*

Appeal from the United States District Court
for the District of Columbia

Before: ROBINSON, RUTH B. GINSBURG and STARR, *Circuit Judges*.

JUDGMENT

This cause came on to be heard on the record and briefs of the parties and was argued by counsel. Upon consideration of the foregoing, it is

ORDERED and ADJUDGED, by the Court, that the judgment of the district court on appeal herein is affirmed, in accordance with the Opinion of the Court filed herein this date.

Per Curiam
For the Court:

/s/ George A. Fisher
GEORGE A. FISHER
Clerk

Date: December 22, 1987

Opinion for the Court filed by Circuit Judge Starr.